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SIPDIS

DEPT PASS USTR FOR KATE DUCKWORTH
DEPT PASS DOC/ITA/MAC/WH/OLAC ANNE DRISCOLL
DEPT PASS TREASURY IA LUYEN TRAN
DEPT PASS NSC GARY TOMASULO AND MIKE SMART

SENSITIVE
SIPDIS

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TAGS: [EINV](#) [ETRD](#) [ECON](#) [EFIN](#) [CVIS](#) [BR](#)
SUBJECT: Brazil: CEO Forum April 28 Scenesetter

Ref a) Brasilia 196 - PAC cable
Ref b) Brasilia 288 - CEOs with Rouseff cable
Ref c) 4/16 erath/DOS-DOC-Treas-NSC e-mail Brazil CEOs with Rouseff
Ref d) Brasilia 289 - investment consolidation cable
Ref e) 4/11 erath/DOS-DOC-Treas-NSC e-mail congress lunch
Ref f) Brasilia 129 - aviation negotiations readout

¶1. (U) This message is sensitive but unclassified, please treat accordingly.

¶2. (U) Summary: The relationship between the United States and Brazil is as productive and broad-based as it has ever been, with an excellent relationship between President Bush and President Luiz Inacio Lula da Silva and new cooperation mechanisms on private sector priorities (CEO Forum), economic policy matters (Economic Partnership Dialogue) and biofuels (March 7 2007 MOU). Regarding CEO Forum priorities, USG and Brazil have had Bilateral Tax Treaty discussions, continued discussions on bilateral investment issues and advanced visa cooperation. USG has also supported workforce development initiatives and other exchanges, helped organize venture capital events, and advanced infrastructure cooperation with Brazil. The CEOs jointly issued a helpful letter urging a "commercially meaningful conclusion" to the WTO Round this year and have worked together on Corporate Social Responsibility initiatives. The April 28 CEO Forum in Washington provides an excellent opportunity for the two governments to showcase our efforts to respond to business priorities and to receive private sector feedback on next steps and new priorities. End Summary.

Brazil Overview

¶3. (SBU) With a 67 percent approval rating, President Lula is more popular than at any other point since he took office in 2003. Continuity and legacy guide the policies of Lula's second term. Lula continues to shape his legacy as a friend of the poor and builder of a foundation for prosperity for the lower and middle classes through broad social welfare programs and a vast, new economic growth program of public works and growth incentives (ref A). At the same time, needed reforms to abolish a political culture of corruption, clientelism, and spoils are lacking. Although a seemingly endless series of corruption scandals has not dented his personal popularity or that of his government, these scandals have felled political allies, including cabinet ministers, in recent years.

¶4. (U) President Lula and his economic team's prudent fiscal and monetary policies and reform efforts are a major reason for his

popularity. Brazil is now the tenth largest economy, with a (diminishing) trade surplus and BB-plus credit rating. Annual GDP growth was 5.4 percent in 2007, with about 4 percent inflation. The currency, the Real, has appreciated against the US dollar by 22 percent since 2006, which has had a dampening effect on Brazilian exports. The strong currency, however, has permitted Brazilian companies to ramp up investment in capital equipment. Foreign Direct Investment in Brazil is increasing, with net flow USD 34.6 billion in 2007 (versus USD 18.8 in 2006). Of total gross inflow of USD 34.3 billion in 2007, USD 6.1 billion came from the United States (number two behind the Netherlands). Brazilian investment in the United States almost tripled between 2001 (USD 1.4 billion) and 2006 (USD 3.9 billion). However, there are major structural challenges to long term growth. Real (as opposed to nominal) interest rates are the highest in the world at 7.1 percent (well ahead of Turkey at 5.6 percent and Australia at 4.6 percent) after Brazil raised its nominal benchmark interest rate from 11.25 percent to 11.75 percent to control inflation. The informal sector constitutes an estimated 40 percent of the economy, in part due to the tax burden (36 percent in 2007), one of the highest among large developing economies. Brazil's opaque and onerous regulatory and legal system, as well as poor transport and other infrastructure, continue to constrain growth.

CEO FORUM PRIORITIES

15. (SBU) TAX TREATY - Information exchange under a BTT continues to be a challenge, both in terms of Brazil's willingness or ability to provide information where there is no Brazilian domestic tax interest and also in terms of the extent of the types of information Brazil would be willing to provide under a treaty. Discussions in Brasilia in March between US and Brazil negotiators indicated that,

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until the Brazilian Supreme Court rules on the constitutionality of information collection under Brazilian complementary law 105, discussions on expanding information collection further to include in cases where no Brazilian domestic tax interest exists can not proceed. A ruling could come in 2008, but is not guaranteed. The OAB (ABA-equivalent) head of the Constitutional Rights Commission believes the Supreme Court will likely rule to permit the current parameters of information collection by Brazil's federal tax authorities, although the head of OAB overall has publicly stated he believes the Supreme Court should rule to constrain information collection for privacy reasons. Within the business community, congress, and even among ministries' officials, ambivalence exists on this issue. Distrust in Receita Federal's ability to safeguard information and suspicions among some that tax authorities mis-collect and mis-use information (fueled by long memories here of scandals past) may impact willingness to press for further information exchange, depending on the types of information requested.

16. (U) In the March session, negotiators had a substantive technical discussion on transfer pricing that increased mutual understanding of each other's systems. The United States side reviewed what USG seeks to achieve in BTTs on limitation of benefits. The Brazilian side expressed conceptual comfort with USG goals in this area. In addition, issues such as tax sparing, taxing source versus recipient, and arbitration also require further discussion. We understand Treasury has invited Receita Federal to Washington for further talks. GOB interlocutors, including Casa Civil, Finance, MDIC and Receita Federal consistently advocate the US take a "step-by-step" approach (as was done with the TIEA) to make incremental progress toward a BTT and to build confidence to make a BTT eventually possible. In the March discussions, both sides agreed to make clear in discussions with the business community that we want to see the TIEA ratified as quickly as possible, but that conclusion of a BTT in the short-term is unrealistic.

17. (SBU) BILATERAL INVESTMENT TREATY - It remains unclear that Brazil would be willing to commit to binding arbitration at the federal, state or municipal level for investor-state disputes. Casa

Civil (Dilma Rousseff) to date believes contract provisions can govern dispute resolution and that an international arbitration mechanism is unnecessary (ref B and C). Discussions with Casa Civil, MRE, Finance, MDIC and CAMEX consistently indicate that, for strategic reasons to increase GoB and congressional confidence in negotiating investment agreements, Brazil prefers to start discussions first with a regional counterpart (ref D and conversations since). In a recent meeting, Finance confirmed Brazil will begin an investment agreement dialogue with Argentina (MRE had wanted to start with a smaller country). Brazilian companies have major investments in Argentina and have experienced significant investment problems, according to our interlocutors. While ministries confirm that the CAMEX-agreed framework that Brazil will use to start its conversation with Argentina does not currently contain any reference to investor-state dispute settlement, some interlocutors are hopeful this element could be introduced over time into this dialogue. We view willingness to engage with Argentina as a positive sign that GoB is beginning to tackle investment agreement conversations; however, we believe both Brazilian and US business as well as USG will need to continue to press in order to convince GoB to engage substantively with us on the provisions of a bilateral investment treaty in the near term.

18. (U) In discussions with key members of the Brazilian Congress, including among others House President Chinaglia, Senator Jereissati (key on tax issues), Senator Maciel (Chair of Senate Constitution and Justice committee; also wrote the 1996 arbitration law), and Senator Fortes (Chair of Senate Foreign Relations), members have indicated openness to further consideration of elements of both investment and tax treaties with the United States, provided that these agreements contain reciprocal commitments and demonstrate clearly the benefits to Brazil (ref E).

19. (U) VISAS - We have proposed to Itamaraty that we drop all visa fees (excepting a uniform processing fee). This will allow us not only to lessen charges on Brazilians, but also to issue combined business/tourist visas as we do in much of the world, saving applicants possible return trips if they apply for one and then find they need the other. We have also proposed that our visa validities for business and tourist be extended to 10 years from five years, which will both benefit our citizens and our visa operations. We are prepared to move on our side. We can drop our fees immediately upon Brazil agreeing to do so. Visa validity extension requires some inter-agency consultation in our government, but no legislative

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action. MRE's legislative proposal to update Brazilian immigration law currently awaits Casa Civil approval and transmission to congress for consideration. If passed as proposed, the legislation would permit Brazil to offer 10 year visas, eliminate the requirement that Brazilian visas must be used within 90 days of issuance, and give MRE more control of its visa processing fees (including the \$60 fee on business visas) (ref B). However, given the slow process on the bill, the MRE recently proposed to the Embassy that we come to a separate agreement covering fees and validity. Such an agreement would still require legislative approval on their side, but MRE officials believe this could be done more quickly than getting the immigration bill approved.

10. (U) Backlogs are still very high, but we have added the first of seven new consular officers and expect all to be in place by July. State Department inspectors recently recommended we add an additional six consular officers to Mission Brazil and we intend to press hard for implementation of that recommendation. We also hope Brazil will be selected to participate in a pilot program to draw on the resources of our Eligible Family Member community to provide more assistance in the consular section. Until we see the effect of the seven new officers and know whether we can add another six and participate in the EFM pilot, it is difficult to predict exactly how much time before we see significant reductions in the backlog.

11. (U) INFRASTRUCTURE - The USTDA Regional Director for Latin America and the Caribbean recently had an excellent series of meetings in Brasilia, Sao Paulo and Rio with Casa Civil, BNDES (Brazil's National Development Bank), state governments and other interlocutors. USTDA is developing a preliminary list of possible

projects with potential for American investment and/or participation (ideas could include areas like port dredging, oil platform water discharge, urban waste management, transportation projects - depending on mutual interest). USTDA has proposed a draft model framework with Casa Civil to structure our cooperation (based on our agreement with India). We expect USTDA will make another visit in the near future to continue this dialogue on possible projects and we are also pursuing the possibility of adding a permanent USTDA person in Brazil. In addition, the Treasury DAS for Latin America visited Brazil to continue dialogue with Casa Civil, Planning Ministry and BNDES officials on how best to structure infrastructure cooperation.

¶12. (U) VENTURE CAPITAL - We've been actively involved over the past 12 months. Activities have included the Institutional Investor Learning Journey (IILJ) in September 2007 where we organized a visit of representatives of 13 US Pension Funds and University Endowments to better understand the Brazilian Economy and its Private Equity and Venture Capital Opportunities; we organized, with ABDI support, the first meeting of the U.S. - Brazil Venture Capital Task Force in March 2008; and we set up two Venture Capital and Entrepreneurship Forums in March 2008, with support from the Kauffman Foundation and ABDI and co-organized by FGV-SP and by PUC-RJ. Planned activities include: FINEP and ABDI are working to select and finance four Brazilian ventures to participate in LARTA's Life Sciences Venture Capital Forum on May 30, 2008 (ABDI has yet to finalize the agreement); and Commerce has proposed that the second meeting of the U.S.-Brazil Venture Capital Task Force take place on August 17, 2008 in Atlanta, to coincide with the second annual Americas Competitiveness Forum (ACF), with ABDI agreement to this in principle.

EXCHANGES AND PROFESSIONAL DEVELOPMENT -

¶13. (U) SCIENTISTS - Brazil has first class scientists and facilities in a number of areas. The U.S. Government (USG) has well-developed scientific cooperative arrangements in two areas with Brazilian counterparts: the Agriculture Research Service of the U.S. Department of Agriculture (USDA/ARS) with EMBRAPA of the Ministry of Agriculture (this includes long-term exchanges of researchers); and the National Institutes of Health with the Ministry of Health, FIOCRUZ (an institution that works with vaccines), and other health institutions. In addition, the National Science Foundation (NSF) and a variety of other U.S. agencies have modest or limited collaborative scientific activities with Brazilian counterparts. Many elements of the U.S. private sector, academia and non-governmental organizations (NGOs) have established scientific ties with Brazilian counterparts. Brazil has demonstrated remarkable scientific and technological prowess in a number of areas, most notably with deep sea oil and gas exploration by PETROBRAS, aviation technology with EMBRAER, and information technology.

¶14. (SBU) TECHNOLOGY EXCHANGE - During Minister of Defense Jobim's
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visit to Washington, the Defense Department proposed a Defense Technology Security Dialogue -an annual meeting between Defense Department and Ministry of Defense experts on technology security issues. The Dialogue would facilitate closer defense cooperation between our countries by creating greater transparency on our countries' technology security policies, procedures and decisions. The Dialogue will enable both sides to exchange information, and to troubleshoot problem issues.

¶15. (U) ENGLISH LANGUAGE STUDY PROGRAM - During Secretary Rice's visit in March to USAID's Enter Jovem program in Salvador, Bahia, Governor Jacques Wagner asked Secretary Rice to help him expand opportunities for youth, particularly through English language instruction, that would help open doors for young people in growing industries. Secretary Rice expressed support for Governor Wagner's initiative. USAID has established a model called the Challenge Fund, whereby USG and private companies can jointly contribute to a development program. A Challenge Fund for English will build upon the success of Enter Jovem in reaching thousands of young people with employment training and subsequent jobs. We have experienced

in Brazil that USAID seed money can leverage very significant amounts of corporate funds, and can also attract support from local governments.

¶16. (U) WORKFORCE DEVELOPMENT AND EDUCATION - Motorola announced recently a \$100,000 grant to USAID's Enter Jovem program, to expand digital inclusion and training to public schools in Bahia. USAID will match the Motorola donation, allowing the program to also expand in Pernambuco, where strong state government support offers the potential to reach many schools and students. Motorola and Enter Jovem will present this model at a Mais Unidos workshop in Sao Paulo on May 12, for the over 60 U.S. companies in our CRS network.

UPDATE ON OTHER AREAS

Biofuels and other Energy Issues

¶17. (U) Since the last CEO Forum, under the March 7, 2007 MOU, NIST, IMMETRO and CEN (the standards bodies for the US, Brazil, and the EU respectively) have issued a joint report laying the foundation for work on biofuels commoditization standards. The Biofuels Steering Committee, with participation of the private sector Advisory Group, met March 3 in Washington. We expect scientists from the United States (including private sector researchers) to come to Brazil this spring, reciprocating Brazilian scientists' September trip to the United States. We have continued cooperative efforts to aid Haiti, El Salvador, St. Kitts and Nevis, and the Dominican Republic in developing their own biofuels capacity. The GOB and USG are pursuing cooperative scientific activities to develop the next generation of biofuels. The more numerous and often better-funded U.S. scientists and laboratories can benefit greatly from this cooperation with Brazil's world-class cadre of scientists and laboratories, which have established an impressive record over the last 30 years.

¶18. (SBU) We anticipate a visit by Energy Secretary Bodman in May and hope to use the opportunity to broaden our energy cooperation beyond biofuels to other areas for expanded collaboration. Brazil hopes to become a leading oil exporter with the development of the recently discovered deep water reserves in the Santos basin, near Sao Paulo. Petrobras, which has been working in the Gulf of Mexico as the world's leader in deep water technology, hopes to capitalize on this find; an interest that has led to worries on the part of U.S. and international oil companies that the government may be trying to set up the parastatal Petrobras to have, if not exclusive, at least primary rights to these new finds. This concern was amplified by the withdrawal of the auction blocks for exploration rights related to this area just before the auction was to take place. Brazil has been a gas importer from Bolivia, a relationship was has been complicated by Morales' unilateral renegotiating of contracts with Petrobras. Brazil also has an unfulfilled contract for gas imports from Argentina, shares its largest hydroelectric dam with Paraguay, and has ongoing conversations with Venezuela's Chavez over a possible gas pipeline and a cooperative oil refinery near Recife, for which despite rhetoric, Petrobras continues to bear the financial costs. Judging by recent talks with GOB officials, more energy cooperation with the U.S. would be welcome.

Civil Aviation

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¶19. (U) US and Brazilian negotiating teams met, for the first time in ten years, in Rio in December. We hope the Sao Paulo parking issue will be favorably resolved by end-May, allowing us to schedule another negotiating round in the latter half of 2008. Increased frequencies, expanded code-share and cargo rights are all issues of importance to the US aviation community (ref F).

SOBEL